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In The

Supreme Court of the United States

October Term, 1992

COMMONWEALTH OF MASSACHUSETTS, et al.,

Petitioners,

v.

GREENWOOD TRUST COMPANY,

Respondent.

On Petition For A Writ Of Certiorari To The United States Court Of Appeals For The First Circuit

BRIEF OF AMICI CURIAE OF THE AMERICAN CONFERENCE OF UNIFORM CONSUMER CREDIT CODE STATES AND THE NATIONAL ASSOCIATION OF CONSUMER CREDIT ADMINISTRATORS IN SUPPORT OF PETITIONERS

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INTEREST OF THE AMICI CURIAE

The American Conference of Uniform Consumer Credit Code States (ACUCCCS) and The National Association of Consumer Credit Administrators (NACCA)[1]

[1] On November 23, 1992 the National Association of Consumer Credit Administrators voted 20-9 (with 2 abstentions) to join this *amici* brief in support of the Petition for Certiorari of the Commonwealth of Massachusetts. Voting in favor were consumer credit administrators from Alabama, Colorado, Connecti-

solicit this Court to grant certiorari because of the destruction of longstanding state consumer protection laws imposed by the preemptive decision of the Court of Appeals for the First Circuit. This decision takes from the states their ability to enforce laws relating to late charges in consumer credit transactions and in one broad stroke expands the ability of credit card issuers to circumvent the substantive consumer credit laws of the states within which they are doing business.

ACUCCCS is an association of states which has adopted in full or substantial part the Uniform Consumer Credit Code in either its 1968 or 1974 versions. Its membership includes Colorado, Indiana, Iowa, Kansas, Maine Oklahoma, South Carolina, Wisconsin and Wyoming. NACCA is a professional association of state consumer credit regulators whose purpose is to improve the supervision of consumer credit laws.

The Amici emphasize that their involvement in this litigation does not represent a condemnation of either credit card late charges or the states who have chosen to

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cut, Iowa, Kentucky, Maine, Massachusetts, Michigan, Mississippi, Missouri, New Hampshire, New Mexico, Oklahoma, Rhode Island, South Carolina (Consumer Finance Division), South Carolina (Department of Consumer Affairs), Texas, Wisconsin, Wyoming and Puerto Rico. Voting against were members from Arizona, Indiana, Kansas, New York, North Carolina, Ohio, Oregon, Virginia and Washington. Regulators from Idaho and Nebraska professed neutrality. A majority of association members also supported the Commonwealth in the two lower court proceedings.

deregulate this area. Some ACUCCCS and NACCA member states allow late charges in open end credit transactions. To the contrary, the Amici seek to uphold the authority of each state to consider, enact and enforce consumer credit laws based on its own economic conditions, and tailored to the needs of its own creditors and consumers. Therefore, it is not Delaware law the Amici object to, rather, it is the application of Delaware law to consumers located in other states who have no representation in Delaware's legislature. These consumers depend upon their own legislatures to implement consumer credit policies that will ensure sufficient availability of credit, place all lenders on an equal competitive footing within the state, and also fulfill the traditional state function of protecting consumer borrowers. These interests are directly jeopardized by Greenwood Trusts's attempt to "nationalize" Delaware law and ignore the consumer credit laws and policies of every other state.

The Amici raised its concerns in this matter at the U. S. District Court and First Circuit and those concerns continue. The expansive definition of interest adopted by the lower court's opinion could result in states losing control over substantive provisions of their consumer protection laws and the inherent police power associated with those laws.

SUMMARY OF THE ARGUMENT

Greenwood Trust through its Discover Card has created a nationwide credit card business. By initiating this action, Greenwood Trust hopes to undermine under the

guise of federal preemption the traditional authority of the state to regulate consumer credit laws. What the Greenwood Trust argument and the decision of the First Circuit fail to understand is that DIDA[2] does not grant such omnipotent authority to a credit card business to avoid state regulation and incorporate other charges into the term "interest". Rather DIDA narrowly addresses the issue of interest rates and preemption of state laws.

The First Circuit's decision also implicitly recognized the propriety of characterizing late charges as a component of the interest rate under the National Bank Act. This dependence on the National Bank Act is misplaced. It only permits national banks to "export" the interest rate of the state where the bank is located; it does not authorize a national bank to assess other charges or terms not permitted by the consumer's home state.

The First Circuit's decision has set up a situation requiring state by state challenges from either the credit card industry or the states themselves to get a clear reading on the status of state law with respect to various credit card terms and charges.

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[2] The Depository Institutions, Deregulation and Monetary Control Act of 1980, Pub. L. No. 96-221, Tit. V. Part C § 521, 94 Stat. 132, 164 ("Section 521").

REASONS FOR GRANTING THE PETITION

I. The Decision of the First Circuit Ignores the Opt Out Provision of DIDA.

When Congress passed DIDA it allowed the states to opt out of the statutory preemption of state usury laws.[3] A number of the Amici states took advantage of the opt out provisions and have overridden all or portions of the preemption.[4]

This option demonstrates that Congress intended to create a narrow window of preemption leaving to the states the opportunity to refuse coverage under DIDA and reestablish their own laws. The entire concept of "opt out" denotes a deference to states' rights and a recognition of the substantive laws protecting consumers that have been initiated by the states. By its actions Congress explicitly recognized that citizens of Wisconsin, for example, should be afforded the consumer protections provided by the laws of the state in which they live. Congress recognized this when Wisconsin's own Senator William Proxmire discussed the ramifications of "opt out" provisions during debate on the Senate floor prior to the law's passage:

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[3] The "opt out" provision to 12 U.S.C.A. § 1831d was codified in the History; Ancillary Laws and Directives at that section under the heading Effective date and application.

[4] Examples of states taking advantage of the preemption include Colorado, Colo. Rev. Stat. Sections 5-13-101 through 105; Maine, Me. Rev. Stat. Ann. tit. 9-A, Sections 1-110; South Carolina, 1981 S.C. Acts 6 Section 3 and 1982 S.C. Acts 385 Section 1; Wisconsin, 1981 Wis. Laws Ch. 45 Section 50.

> The presumption [sic] of usury laws does not derogate state authority. Under usury provisions, each State may reimpose its usury limits, if it so desires. We do not take that away from the States. They can put those usury laws back into effect. 126 Cong. Rec. 7070 (1980).

The "opt out" provision recognizes that a state has a right to control its own destiny in the protection of consumers and that no other state has a right to impose its legislative philosophy on another.

It is inconceivable that Congress would not have enacted Section 525 enabling the states to override usury preemption and on the other hand enacted Section 521 in the same part of the same title, intending it to allow states to have a free hand to define "interest rate" so as to reimpose the very terms on other states that had opted out.

II. "Interest" Does Mean Numerical Percentage Rate and is not an All Encompassing Term.

The First Circuit holding has concluded summarily that DIDA's use of the term "interest" buttressed by selected dictionary definitions, means more than "interest." To the court "interest" now means late fees and possibly overlimit fees, NSF check charges and virtually any other theory a credit card issuer can concoct to rationalize how it sets its annual percentage rate.

This expansive definition violates Congress' intent. In DIDA the word "interest" was consistently modified by the word "rate". The states recognize this fact. Since

the inception of DIDA states that have wanted to incorporate other fees into their definition of "interest" have noted the need to pass legislation to do so. This includes the state of Delaware, home of Greenwood Trust.[5] Since the term "interest" by itself could not include other charges and terms, some states have redefined the term for their own purposes.

Consequently, the lower court's decision jeopardizes the dual system of banking which has operated in various forms since the beginning of the United States. In contrast, Congress has historically adopted a conscious policy of "equalization" acknowledging the authority of each state to design the permissible structure for banks, whether state or nationally chartered which were domiciled in the state.[6] The states have individually made determinations on what interest rates and additional charges could be assessed.

These choices go to the states' capacity to determine how the financial industry will affect its citizens and what rights, protection and responsibilities will be afforded to both industry and the citizenry. The dual

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[5] States that have incorporated other charges into their definition of "interest" since the advent of DIDA include: Del. Code Ann. tit. 5, §§ 945, 955 (1988); Ohio Rev. Code Ann. § 1107.262 (Baldwin 1991); La. Rev. Stat. Ann. § 6:548 (1990); Ga. Code Ann. § 7-5-4 (1990).

[6] See Federal Reserve Act of 1913 (Act of Dec. 23, 1913, Ch. 6 Stat. 251); *Lewis v. Fidelity & Deposit Co.*, 292 U.S. 559, 564-65 (1934) which noted incorporation of state law into the National Bank Act as the standard for regulating national banks to ensure competitive equality.

banking system has been defended as representing Federalism in practice by providing flexibility to the states and encouraging experimentation and innovation at the state level.[7] Furthermore the dual system provides "checks and balances against over-regulation by a single monolithic regulatory body.[8]

The First Circuit decision does not adequately recognize how this country's dual banking system is rooted in concepts of federalism and state sovereignty. For example, the lower court's reliance on the National Bank Act is misplaced. In addition, the National Bank Act was enacted 116 years before the statute at issue. The purpose behind the two differ significantly. Congress' intent in the 1860's to set up a unified currency system and prevent discrimination against national banks is vastly different from Congress' attempt in 1980 to resolve a credit availability crisis.

Even assuming for the moment that DIDA allows state chartered institutions all of the same rights as the National Bank Act, Congress never intended for contractual terms such as late charges to be exportable as a component of the "interest rate." In Section 501, a companion provision to Section 521, the clear and unequivocal legislative history dealing with usury law preemption in mortgage loans shows that Congress did not intend to

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[7] See, Note, *The Federal Bank Commission Act: A Proposal to Consolidate the Federal Banking Agencies,* 25 Clev. St. L. Rev. 475, 478-492 (1976).

[8] *Id. See Also* Golembe, *Our Remarkable Banking System,* 53 Va. L. Rev. 1091 (1967).

preempt through DIDA the States' ability to limit late charges:

> In exempting mortgage loans from state usury limitations, the Committee intends to exempt only those limitations that are included in the annual percentage rate. The Committee does not intend to exempt limitations on prepayment charge, attorney fees, late charges or similar limitations designed to protect borrowers.
>
> S. Rep. No. 368, 1st Sess. 19 (1979), reprinted in (1980) U.S. Code Cong. & Admin. News 236, 255.

Beyond this clear indication of Congressional intent in DIDA, the characterization of late charges as a component of the interest rate is totally inconsistent with 12 U.S.C. § 85.

The clear language of that section of the National Bank Act indicates that in transactions other than business or agricultural loans, a national bank has a choice between the rate allowed by the laws of the state or territory or a rate of one percent in excess of the discount rate on ninety-day commercial paper available at the Federal Reserve bank in the national bank's district. The penalty provisions in 12 U.S.C. § 86, based on traditional state usury penalties, imply that a maximum as between the two alternative rates exists, the violation of which leads to the federal usury penalty of the forfeiture of all interest provided for as well as a return of twice the amount of interest already collected. Numerous cases

establish that banks must calculate the correct maximum rate or face liability.[9]

Moreover, Congress gave national banks alternative rates so that the higher of the rates be considered the rate maximum. A fortiori, Congress also intended that a national bank should be reasonably able to determine which of the alternative rates were higher, and likewise, how to calculate them.

If contractual terms such as late charges can properly be considered a component of the interest rate, this would be true whether or not there were affirmative limitations on the interest rate. In any event, States such as Delaware and South Dakota have attempted to legislate not only that rates are unlimited, but that many other contractual terms are part of the interest rate.[10]

Nevertheless, unless a state resorts to the expedient of totally deregulating rates and terms, national banks are

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[9] See e.g. *Citizens National Bank v. Donnell*, 195 U.S. 369 (1904); *Lake Benton First National Bank v. Watt*, 184 U.S. 151 (1902); *Partain v. First National Bank of Montgomery*, 467 F. 2d 167 (5th Cir. 1972).

[10] States such as Delaware and South Dakota have the right to deregulate rates for their own citizens and the Amici do not dispute this right. By the same token, their populations are relatively small, and their laws are designed to maximize the extra-territorial effect of their laws on the citizens of other States through exportation. In the same title Delaware attempts to minimize the effect card issuing banks could have on local competition by limiting other areas of banking activity. See Del. Code Ann. tit. 5, §§ 1001-1056 (1983). See also *Independent Comm. Bankers Ass'n. of South Dakota v. Bd. of Governors of the Federal Reserve System*, 838 F. 2d 969 (8th Cir. 1988).

exposed to liability under 12 U.S.C. § 86 if they calculate incorrectly.

Unlike origination charges or other prepaid finance charges which may be calculated into the annual percentage rate so that it may be expressed as a numerical rate (as is specifically recognized in the Truth in Lending Act at 15 U.S.C. §§ 1605 (a)(1) and 1606), late charges are necessarily unknown at the time the loan is consummated. Thus, a fixed interest rate which considered late charges as a component would be rendered incalculable, both because of the inability to determine in advance how many late charges might be paid and because of the inability to compare the "most favored lender rate" with the federal discount rate set forth in 12 U.S.C. § 85 to determine which is actually higher.

III. The Decision of the First Circuit Incorrectly Preempts the State Police Powers.

If late charges amount to interest rates, then other charges and other substantive provisions may be so considered. Indeed, Greenwood Trust urges, and the First Circuit appears to hold, that other consumer protection statutes may be preempted to the extent that the consumer protection affect the creditor's bottom line, its "cost of lending." (App. A-25). Examples could include attorney fees, default charges of all sorts, garnishment protection provisions, prepayment penalty restrictions and so forth.

Moreover, it appears that even if such terms would not ordinarily be regarded as within the definition of interest rate, a card friendly state legislature is free to

characterize them as interest rate components. Suppose in State X credit card exporting banks decide it is an inconvenience to send notices and comply with the debt collection restrictions of the other states in which its customers live. Suppose further that it prevails on the legislature of State X to define interest rate to include debt collection procedures. Lenders may use the expansive definition adopted by the lower court to argue they now have the right to ignore state law regulating collection practices.

To use the First Circuit's analogy, the train which it has put on the tracks has no brakes, and there is no predicting how far it will go down the tracks preempting state consumer protection laws. The concerns of the Amici are not fanciful or abstract. Using the "exportation" theory, creditors have already refused to comply with Amici state laws in the following areas:

1) Private label cards (merchant credit cards, issued in the name of and with the logo of the merchant, nominally financed or serviced through an out of state bank);

2) Tax refund loans (electronically filed tax returns are prepared and/or brokered by local merchants, but an out of state bank is the source of the funds);

3) Secured card scams (credit cards secured by a deposit in an out of state bank, aimed at persons with bad credit, and in which the profit is made by excessive fees and charges assessed outside the annual percentage rate); and

4) Vehicle manufacture card (credit cards issued by a vehicle manufacturer's captive national bank).

It is difficult to imagine a form of consumer lending that a creditor could not allege some nominal connection with a federally insured bank such that preemption could be claimed. The difference between a vehicle manufacturer's credit card and typical dealer financing by assignment to the manufacturer's acceptance company is essentially a difference in form only.

If the First Circuit's construction of Section 521 is correct, Congress could have simply decreed that "no state shall make any law restricting the rates or terms of consumer credit." However, Congress did not do so. Given Congress' extensive efforts in DIDA to show deference to states' regulatory authorities, this was clearly not Congress' intent.

The First Circuit seems bent on beginning with an assumption that there is in fact federal preemption in this case. The First Circuit ignores the beginning of the analysis of whether there is preemption. The Court has stated when considering preemption, "we start with the assumption that the historic police powers of the states were not to be superseded by the Federal Act unless that was made the clear and manifest purpose of Congress." *Rice v. Santa Fe Elevator Corp.*, 331 U.S. 218, 230 (1947).

The First Circuit would have been better served to follow the words of Justice Blackmun who stated:

> The principles of federalism and respect for state sovereignty that underlie the Court's reluctance to find pre-emption where Congress has not spoken directly to the issue apply with equal force where Congress has spoken, though ambiguously. In such cases, the question is not *whether* Congress intended to pre-empt state regulation, but to what *extent*. *Cipollone v. Ligget*

Group, Inc. 112 S. Ct. 2608, 2626 (1992) (concurring in the judgement in part, and dissenting in part) (emphasis in the original).

The effect of the First Circuit's decision on the states' longstanding and recognized role in consumer credit is particularly troublesome to the amici who are charged with regulating credit transactions and protecting consumers.[11]

If the First Circuit decision is allowed to stand, consumers could be subject to the whims of creditors in foreign states. This is not just conjecture. There has been at least one case filed in the credit card issuer's home state against an out of state cardholder for being in default according to the laws of the state of the card issuer rather than the state of the cardholder.[12] The cardholder was not to be afforded the protections of his home state's substantive consumer protection and credit laws. The Amici strongly believe that Congress did not intend this result. State residents deserve the protection of their own state's laws and should not be generally subject to the laws of other states whose only protections are those offered to the credit card industry.

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[11] See *Aldens, Inc. v. Packel*, 524 F. 2d 38, 46 (3d Cir. 1975), *cert. denied*, 425 U.S 943 (1976); *Griffith v. Connecticut*, 218 U.S. 563, 568-569 (1910); *General Motors Corp. v. Abrams*, 897 F. 2d 34, 41-42 (2d Cir. 1990); *Motor Vehicles Mfrs. Ass'n of U.S., Inc. v. Abrams*, 899 F. 2d 1315, 1319 (2nd Cir. 1990), *cert. denied* 111 S. Ct. 1122 (1991); *Chrysler Corp. v. Texas Motor Vehicle Com'n*, 755 F. 2d 1192, 1205 (5th Cir. 1985).

[12] *Bank One Columbus NA v. Kerry L Dutton 2104 Piedmont Road, Eau Claire, Wi. 54703* M 9110CVF-037052 (Franklin County, Ohio Municipal Court 1991).

CONCLUSION

The train the First Circuit mentioned is a runaway which has lost all recognition of stopping at the station of states' rights. The different states laws are not inconsistent with the federal law. The state laws may be inconsistent with each other, however, Congress did not intend and federal law should not be used as a mechanism to preempt one state's laws at the expense of another.

For these reason ACUCCCS and NACCA respectfully request this Court to grant the Commonwealth's petition for writ of certiorari.

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